

## FALSE CLAIMS ACT LAWSUITS: “NEW” FOCUS ON MATERIALITY

On June 16, 2016, the United States Supreme Court issued its decision in *Universal Health Services, Inc. v. United States ex rel. Escobar*, a False Claims Act (“FCA”) case reviewing the theory of implied certification, which was subject to a circuit court split. In the opinion, the Court upheld the viability of the implied certification theory as a basis for a FCA suit but replaced former distinctions between express and implied certification and conditions of payment/conditions of participation with a “new” materiality standard. Takeaways for providers under the materiality standard include the following.

- Providers could technically violate a condition of payment, but such violation, if not material, may not rise to the level of a false claim; and
- Providers could violate conditions of participation or other requirements previously not characterized as conditions of payment, but such violations, if material, may now be considered to be false claims.

### BACKGROUND

The Plaintiffs in *Escobar* alleged that a mental health facility had submitted claims to the Massachusetts Medicaid program for services that the facility knew had been provided by individuals without the proper licensure. Even though the facility never expressly represented that those individuals were licensed, Plaintiffs alleged that the facility’s Medicaid claims were impliedly false and actionable under the FCA due to the facility’s failure to disclose the lack of the required licenses to the Medicaid program. The District Court originally granted Defendants’ motion to dismiss for failure to state a claim, finding that licensure was not a condition of payment, which the court determined was a requirement under the implied certification theory. The United States Court of Appeals for the First Circuit reversed the District Court’s decision, finding that conditions of payment need not be expressly designated by the government. The First Circuit determined that the licensure requirements were in fact conditions of payment under Massachusetts Medicaid, and, therefore, the District Court was incorrect to dismiss the case.

### ANALYSIS

Resolving the circuit court split regarding the application of the implied certification theory, the Supreme Court emphasized the importance of the FCA’s materiality standard. The Court rejected previous limitations on the scope of falsity that some courts had fashioned but defined materiality (relying upon common law principles as well as the statute) in such a manner that makes abundantly clear that not every violation of either an express or implied certification, or every false statement, would be actionable. Stating that nothing in the text of the FCA restricts its scope to violations of conditions of payment, the Court placed the focus on whether compliance with the requirement that was violated was “material to the Government’s payment decision...” With regard to the FCA’s materiality requirement, the Court stated that “[t]he materiality standard is demanding,” that “materiality looks to the effect on the likely or actual behavior of the recipient of the alleged misrepresentation” and that a “misrepresentation is material only if it would likely induce a reasonable person to manifest his assent” (internal citations omitted). The Court also provided factors to consider when determining materiality under the FCA, finding that:

- The fact that a requirement is deemed a condition of payment is not sufficient to determine materiality, although it is relevant;
- The fact that a requirement is not deemed a condition of payment is not sufficient to conclude the requirement is not material;
- Knowledge by the defendant that the government has consistently refused to pay the type of claims in question based on noncompliance with statutory or regulatory requirements supports materiality; and
- Demonstrating that the government has paid the type of claims in question despite having knowledge of such violations is evidence against materiality.

In addition to materiality, the Court also said that under the implied false certification theory, claims must do more than simply request payment: they must also make specific representations about the underlying goods or services provided and to be reimbursed, and such representations are delinquent in some manner that “makes those representations misleading half-truths.” The Court defines “misleading half-truths” as “representations that state the truth only so far as it goes, while omitting critical qualifying information.” These standards

comport with common law fraud principles, which largely informed the Court's interpretation of the FCA and its decision.

## **PRACTICAL TAKEAWAYS**

While much remains to be interpreted through future decisions, initial takeaways from *Escobar* include the following:

- Under the materiality standard, the landscape as to what may be considered a false claim under the FCA could shift significantly as courts and the government determine which requirements are material;
- Providers have an opportunity to more proactively defend lawsuits that are based on technical or relatively minor omissions. The Court recognized the “thousands of complex statutory and regulatory provisions” that providers are subject to and that allowing FCA suits to proceed based on *any* violation of conditions of payment would hinder providers from prioritizing the more important compliance obligations;
- Technical violations of the Stark Law or other statutes may no longer rise to the level of a false claim if they are not considered to be material; and
- While receiving less attention than materiality at the moment, the Court's determination that representations must rise to the level of “misleading half-truths” will likely be an important and heavily contested issue going forward.

If you have any questions regarding the impact of the *Escobar* decision, or on the FCA in general, please contact:

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